

ORIGINAL

NEW APPLICATION



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BEFORE THE ARIZONA CORPORATION COMMISSION

FEB - 1 P 12: 06

COMMISSIONERS

BOB STUMP, Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

Arizona Corporation Commission

DOCKETED

FEB - 7 2013

DOCKETED BY

nr

ARIZONA CORPORATION COMMISSION
SECRET CONTROL

IN THE MATTER OF THE APPLICATION OF
GRAHAM COUNTY UTILITIES, INC. GAS
DIVISION FOR APPROVAL OF A LOAN

DOCKET NO. G-02527A-13-0023

FINANCE APPLICATION

Pursuant to A.R.S. § 40-301 et seq., Graham County Utilities, Inc. Gas Division ("GCU"), hereby files with the Arizona Corporation Commission ("Commission") an Application ("Finance Application") for authorization to borrow \$1,000,000 from the Graham County Electric Cooperative ("GCEC") to finance prior construction of plant in accordance with GCU's construction work plan and establish a \$500,000 line of credit with GCEC to address future capital needs. In support of its Finance Application, GCU states as follows:

1. GCU and GCEC are non-profit corporations and public service corporations.

GCU holds a Certificate of Convenience and Necessity, to provide Gas Distribution Service to its member-customers in Graham County, Arizona. GCEC holds a Certificate of Convenience and Necessity, to provide Electric Distribution Service to its member-customers in Graham County, Arizona.

2. The Commission has jurisdiction over GCU and GCEC and the subject matter of this Finance Application.

1 3. GCU currently provides gas service to approximately 5,393 members.

2 4. On February 6, 2013, GCU's and GCEC's Board of Directors approved a
3 Resolution for a loan from GCEC in the amount of \$1,000,000, to finance prior construction of
4 plant and a \$500,000 LOC to fund future capital needs. GCU has attached to this application a
5 schedule showing the net plant additions for the years 2008 through 2011. Among other things,
6 GCU expended funds on new gas mains, services, meters and regulators and miscellaneous
7 distribution equipment to improve and work on the gas distribution system. Graham County
8 Electric Cooperative Inc. ("GCEC") has provided temporary financing to GCU for these plant
9 additions. GCU will be using the Loan from GCEC to repay GCEC for funds that it has advanced
10 to GCU. GCU will be using the LOC to fund additional/future capital investments.

11
12 5. GCU is submitting an application for long-term financing in the amount of
13 \$1,000,000, with a maturity date to cover a period of ten (10) years and with fixed interest rate of
14 5.44 percent, to fund the construction of the facilities identified in GCU's schedule of net plant
15 additions.

16
17 6. As a part of this application, GCU is requesting a LOC in the amount of \$500,000,
18 with no maturity date and with a variable interest rate equal to the rate charged by the National
19 Rural Cooperative Finance Corporation ("CFC") for an intermediate LOC (currently
20 approximately 2.9 percent) to fund the future construction of facilities and financial
21 contingencies. GCU would use the LOC to fund immediate capital needs as bridge financing
22 that may be re-financed using a longer term loan upon ACC approval.

23
24 7. A copy of the GCU and GCEC Board of Directors' resolution approving the Loan
25 and LOC Application is attached here to.

26

1 8. GCU intends to repay, in substantial part, the cost of the Loan
2 over a ten (10) year period and LOC through the use of its general funds. On July 13, 2012, GCU
3 has filed an application for a rate case for the Gas Division in Docket No.G-02527A -12-0321.
4 GCU requests that this financing application be consolidated with the pending rate case docket.
5 Due to GCU's poor financial condition, GCU further requests that this application be processed
6 concurrently with the rate case application and not delay the rate case application time clock.
7

8 9. GCU's Loan and LOC request is: (1) for lawful purpose; (2) within
9 GCU's corporate powers; (3) compatible with the public interest; (4) within sound financial
10 practices; and (5) within the proper performance of the Cooperative as a public service
11 corporation. The Loan and LOC will improve GCU's ability to continue to provide safe and
12 reliable gas distribution service to its member-customers.
13

14 10. The Loan and LOC are dependent upon authorization by this Commission.

15 11. The aggregate amount of securities outstanding, and proposed to be
16 outstanding, will not exceed the fair value of GCU's properties and business. A copy of GCU's
17 audited financial statements for the years ended September 30, 2010 and 2011 is also attached
18 here to.

19 12. GCU requests that the Commission act on this application as soon as possible to
20 assist GCU financially to maintain reliable gas distribution service.
21

22 13. All correspondence with regard to this Finance Application should be
23 sent to:

24 John V. Wallace
25 Grand Canyon State Electric Cooperative Association, Inc.
26 2210 South Priest Drive
 Tempe, Arizona 85282
 E-mail: jwallace@gcseca.coop

1 With a copy to:

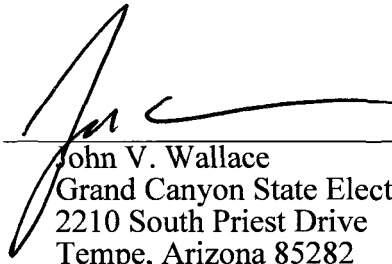
2 Kirk Gray
3 GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
4 P. O. Drawer B
5 Pima, Arizona 85543
6 Email: kgray@gce.coop

7 WHEREFORE, GCU, having fully stated its Application and showing
8 that it is in the public interest for the Cooperative to obtain the Loan to fund prior construction of
9 facilities to serve its member-customers and to obtain a LOC for future capital needs, hereby
10 requests that the Commission:

- 11 1. Accept GCU's Finance Application for filing.
- 12 2. Consolidate the Finance Application with the pending rate case (Docket No.G-
13 02527A -12-0321).
- 14 3. Due to GCU's poor financial condition, GCU further requests that this application
15 be processed concurrently with the rate case application and not delay the rate case
16 application time clock.
- 17 4. Authorize GCU to borrow \$1,000,000 from GCEC for the lawful purposes set
18 forth in this Finance application and establish a \$500,000 LOC with GCEC, and to
19 authorize the Cooperative to take such actions necessary and appropriate to
20 execute a mortgage to secure the Loan and LOC; and
21 5. Grant such other relief as may be in the public interest.
- 22
- 23
- 24
- 25
- 26

1 RESPECTFULLY SUBMITTED this 7th day of February 2013.

2
3
4 By


John V. Wallace

Grand Canyon State Electric Cooperative Association, Inc.
2210 South Priest Drive
Tempe, Arizona 85282

5
6
7
8
9
10 Original and thirteen (13) copies of
11 GCU's Financing Application
12 filed this 7th day of February, 2013
13 with:

14 DOCKET CONTROL
15 Arizona Corporation Commission
16 1200 West Washington Street
17 Phoenix, Arizona 85007
18
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GRAHAM COUNTY UTILITIES, INC. - GAS
SCHEDULE OF PLANT
TEST FISCAL YEAR SEPTEMBER 30, 2011

ACCOUNT #	DESCRIPTION	9/30/2006	NET ADDITIONS	9/30/2007	NET ADDITIONS	9/30/2008	NET ADDITIONS	9/30/2009	NET ADDITIONS	9/30/2010	NET ADDITIONS	BALANCE 9/30/11
2301.00	ORGANIZATION	42,522		42,522		42,522		42,522		42,522		42,522
2374.00	LAND & LAND RIGHTS	1,494		1,494		1,494		1,494		1,494		1,494
2376.00	MAINS	1,593,823	62,074	1,655,897	109,129	1,765,026	59,673	1,824,699	158,268	1,982,967	226,765	2,209,732
2380.00	SERVICES	697,194	44,552	741,746	50,949	792,695	22,077	814,772	94,688	909,460	181	909,641
2381.00	METERS & REGULATORS	910,135	70,385	980,520	81,024	1,061,544	63,230	1,124,774	99,135	1,223,909	42,301	1,266,210
2390.00	STRUCTURES & IMPROVEMENTS	3,309		3,309		3,309		3,309		3,309		3,309
2391.00	OFFICE EQUIPMENT	2,750		2,750		2,750		2,750		2,750		2,750
2392.00	TRANSPORTATION EQUIPMENT											
2394.00	TOOLS, SHOP & GARAGE EQUIPMENT	93,304	10,107	103,411	21,120	124,531	(1,741)	122,790		122,790	9,786	132,576
2396.00	POWER OPERATED EQUIPMENT	6,000		6,000	57,887	63,887	2,122	66,009		66,009		66,009
	TOTAL	3,350,531	187,118	3,537,649	320,109	3,857,758	145,361	4,003,119	352,091	4,355,210	279,033	4,634,243

RECONCILIATION TO GENERAL LEDGER

PER GENERAL LEDGER	3,506,173	187,118	3,693,291	320,109	4,013,400	145,361	4,158,761	352,091	4,510,852	279,033	4,789,885
LESS: ACQUISITION ADJUSTMENT	(415,485)		(415,485)		(415,485)		(415,485)		(415,485)		(415,485)
PLUS: PORTION OF ACQ. ADJ. USED FOR PLANT (1)	259,843		259,843		259,843		259,843		259,843		259,843
NET	3,350,531	187,118	3,537,649	320,109	3,857,758	145,361	4,003,119	352,091	4,355,210	279,033	4,634,243

ACCOUNT # DESCRIPTION

2108.60	ACCUM PROV FOR DEPR - DIST PLANT	1,564,567	98,843	1,415,649	104,792	1,768,202	111,306	1,879,508	119,953	1,999,461	130,314	2,129,775
2108.70	ACCUM PROV FOR DEPR - GENERAL PLANT	96,953	8,926	80,435	15,278	121,157	16,353	137,510	16,316	153,826	16,705	170,531
	TOTAL	1,661,520	107,769	1,496,084	120,070	1,889,359	127,659	2,017,018	136,269	2,153,287	147,019	2,300,306

RECONCILIATION TO GENERAL LEDGER

PER GENERAL LEDGER	1,823,740	117,205	1,639,430	129,506	2,070,451	137,095	2,207,546	145,705	2,353,251	156,455	2,509,706
LESS: ACQUISITION ADJUSTMENT	(282,530)	(16,619)	(249,290)	(16,619)	(315,768)	(16,619)	(332,387)	(16,619)	(349,006)	(16,619)	(365,625)
PLUS: PORTION OF ACQ. ADJ. USED FOR PLANT (1)	120,310	7,183	105,944	7,183	134,676	7,183	141,859	7,183	149,042	7,183	156,225
NET	1,661,520	107,769	1,496,084	120,070	1,889,359	127,659	2,017,018	136,269	2,153,287	147,019	2,300,306

(1) PER DECISION NO. 58437

**GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
GRAHAM COUNTY UTILITIES, INC.**

**BOARD RESOLUTION AUTHORIZING LONG TERM FINANCING AND A LINE OF
CREDIT TO GRAHAM COUNTY UTILITIES, INC.**

WHEREAS, the Board of Directors of Graham County Utilities, Inc. (GCU) has requested long term financing for prior gas construction of plant and a line of credit agreement with Graham County Electric Cooperative, Inc., (GCEC).

WHEREAS, GCEC has determined that it will authorize long term financing and establish a line of credit to GCU.

Total Long Term Financing Requested by GCU: \$1,000,000.00
Total Line of Credit Requested by GCU: \$500,000.00

NOW, THEREFORE BE IT RESOLVED, that Graham County Utilities, Inc., (Gas Division) be authorized to borrow \$1,000,000.00 from Graham County Electric Cooperative, Inc. (GCEC) to be used for financing prior gas construction of plant.

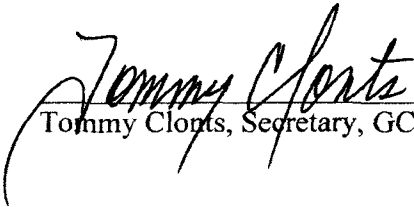
BE IT ALSO RESOLVED, that the financing shall provide for the repayment of the Loan; in monthly installments, including interest and principal payments. The term of the loan will be ten (10) years and the interest rate will be 5.44 percent.

BE IT ALSO RESOLVED, that the line of credit in the amount of \$500,000.00 shall be established between GCEC and GCU with no maturity date and with a variable interest rate equal to the rate charged by the National Rural Cooperative Finance Corporation (CFC) for an intermediate line of credit.

BE IT FURTHER RESOLVED, that the management be authorized to file with the Arizona Corporation Commission an application requesting financing.


IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of Graham County Electric Cooperative, Inc., this 6th day of February, 2013.

CORPORATE SEAL


Tommy Clonts, Secretary, GCEC

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of Graham County Utilities, Inc., this 6th day of February, 2013.

CORPORATE SEAL


Michael K. Crockett, Secretary, GCU

GRAHAM COUNTY UTILITIES, INC.

PIMA, ARIZONA

FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION

FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

LUBBOCK, TEXAS

GRAHAM COUNTY UTILITIES, INC.

PIMA, ARIZONA

FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION

FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

**GRAHAM COUNTY UTILITIES, INC.
PIMA, ARIZONA**

**FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010**

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BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

PHONE: (806) 747-3808

FAX: (806) 747-3815

8215 NASHVILLE AVENUE

LUBBOCK, TEXAS 79423-1954

INDEPENDENT AUDITORS' REPORT

Board of Directors
Graham County Utilities, Inc.
Pima, Arizona

We have audited the accompanying balance sheets of Graham County Utilities, Inc. (the Cooperative), as of September 30, 2011 and 2010, and the related statements of income and accumulated margins, and cash flows for the years then ended. These financial statements are the responsibility of the Cooperative's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Graham County Utilities, Inc. as of September 30, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 22, 2011, on our consideration of the Cooperative's internal control over financial reporting and on its compliance with certain provision of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

Bolinger, Segars, Gilbert & Moss L.L.P.

Certified Public Accountants

November 22, 2011

FINANCIAL STATEMENTS

-2-
GRAHAM COUNTY UTILITIES, INC.

Exhibit A

BALANCE SHEET
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010

ASSETS

	September 30,	
	2011	2010
UTILITY PLANT		
Plant in Service	\$ 7,928,538	\$ 7,472,982
Construction Work in Progress	436,018	589,566
Plant Acquisition Adjustment	<u>1,025,652</u>	<u>1,025,652</u>
	\$ 9,390,208	\$ 9,088,200
Less: Accumulated Provision for Depreciation and Amortization	<u>4,672,504</u>	<u>4,395,875</u>
	<u>\$ 4,717,704</u>	<u>\$ 4,692,325</u>
OTHER PROPERTY AND INVESTMENTS		
Investments in Associated Organizations	\$ 319,797	\$ 234,833
CURRENT ASSETS		
Cash - Restricted	\$ 52,725	\$ 46,648
Accounts Receivable (Less allowance for uncollectibles of \$76,993 in 2011 and \$84,544 in 2010)	84,531	40,161
Materials and Supplies	134,048	147,415
Other Current and Accrued Assets	<u>30,777</u>	<u>35,663</u>
Total Current Assets	<u>\$ 302,081</u>	<u>\$ 269,887</u>
DEFERRED CHARGES	\$ 43,088	\$ 50,788
TOTAL ASSETS	<u>\$ 5,382,670</u>	<u>\$ 5,247,833</u>

EQUITIES AND LIABILITIES

MEMBERS' EQUITY		
Memberships	\$ 31,292	\$ 31,354
Accumulated Margins (Deficits)	<u>(349,918)</u>	<u>(427,859)</u>
	<u>\$ (318,626)</u>	<u>\$ (396,505)</u>
LONG-TERM DEBT		
CFC Mortgage Notes Less Current Maturities	\$ 2,002,092	\$ 2,213,105
USDA Rural Development Note Payable Less Current Maturities	1,486,395	1,510,766
CIAC Refund Due	<u>88,151</u>	<u>154,189</u>
	<u>\$ 3,576,638</u>	<u>\$ 3,878,060</u>
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 373,014	\$ 293,076
Accounts Payable - Other	82,111	82,099
Accounts Payable - Graham County Electric Coop	1,260,814	834,642
Overbilled Consumers Fuel Cost	230,169	378,378
Customers' Deposits and Prepayments	78,750	77,625
Accrued Taxes	57,453	58,299
Accrued Interest	19,923	19,506
Accrued Payroll	<u>22,424</u>	<u>22,653</u>
Total Current Liabilities	<u>\$ 2,124,658</u>	<u>\$ 1,766,278</u>
TOTAL EQUITIES AND LIABILITIES	<u>\$ 5,382,670</u>	<u>\$ 5,247,833</u>

See accompanying notes to financial statements.

GRAHAM COUNTY UTILITIES, INC.

Exhibit B

STATEMENT OF INCOME AND ACCUMULATED MARGINS
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010

	September 30,	
	2011	2010
OPERATING REVENUES	\$ 4,054,110	\$ 3,804,753
OPERATING EXPENSES		
Purchased Gas	\$ 1,399,908	\$ 1,644,748
Power for Pumping	54,478	49,922
Operations	439,780	368,856
Maintenance	545,659	464,199
Consumer Accounts	409,213	369,921
Administrative and General	590,172	672,726
Depreciation and Amortization	276,629	264,260
Other Interest	61,333	79,283
Total Operating Expenses	\$ 3,777,172	\$ 3,913,915
OPERATING MARGINS (DEFICIT) - BEFORE FIXED CHARGES	\$ 276,938	\$ (109,162)
Interest on Long-Term Debt	213,719	174,908
OPERATING (DEFICIT) - AFTER FIXED CHARGES	\$ 63,219	\$ (284,070)
Capital Credits	14,645	16,703
NET OPERATING (DEFICIT)	\$ 77,864	\$ (267,367)
NONOPERATING MARGINS		
Interest	77	457
NET MARGINS (DEFICIT)	\$ 77,941	\$ (266,910)
ACCUMULATED DEFICIT - BEGINNING OF YEAR	(427,859)	(160,949)
ACCUMULATED DEFICIT - END OF YEAR	\$ (349,918)	\$ (427,859)

See accompanying notes to financial statements.

GRAHAM COUNTY UTILITIES, INC.

Exhibit C

STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010

	September 30,	
	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Margin (Deficit)	\$ 77,941	\$ (266,910)
Adjustments to Reconcile Net Margins to		
Net Cash Provided by Operating Activities		
Depreciation and Amortization	276,629	264,260
Capital Credits - Noncash	(7,322)	(5,485)
Over/(Under)billed Fuel Cost	(148,209)	130,849
Deferred Charges	7,700	(10,560)
Accounts Receivable	(44,370)	(5,006)
Inventories and Other Current Assets	18,253	(15,173)
Payables and Accrued Expenses	479	8,616
Net Payments (to) from - Graham County Electric Cooperative	426,172	(505,518)
Net Cash Provided by (Used in) Operating Activities	\$ 607,273	\$ (404,927)
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Plant	\$ (302,008)	\$ (644,873)
Cash - Restricted	(6,077)	(69)
Investments in Associated Organizations	(77,642)	8,704
Net Cash Used in Investing Activities	\$ (385,727)	\$ (636,238)
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances on Long-Term Debt from CFC	\$	\$ 1,050,000
CIAC Refund Due		226,765
Payments on Note Payable to AEPCO		(25,667)
Payments on Long-Term Debt to CFC	(198,013)	(172,865)
Payments on Long-Term Debt to GCEC		(14,607)
Payments on Long-Term Debt to USDA	(23,471)	(22,736)
Memberships	(62)	275
Net Cash Provided by (Used in) Financing Activities	\$ (221,546)	\$ 1,041,165
CHANGE IN CASH	\$ 0	\$ 0
CASH - BEGINNING OF YEAR	0	0
CASH - END OF YEAR	\$ 0	\$ 0
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash Paid During the Year for:		
Interest on Long-Term Debt	\$ 213,719	\$ 174,908
Federal Income Tax	\$ 0	\$ 0

See accompanying notes to financial statements.

-5-
GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Graham County Utilities, Inc. (the Cooperative) is organized as a cooperative to provide gas and water utility services to customers in Graham County, Arizona. The Cooperative was incorporated February 14, 1989, and began operations in November, 1989, with the purchase of assets and liabilities from two private utility companies. The Cooperative has been granted exemption from Federal income taxes under Internal Revenue Code Section 501(c)(12).

Basis of Accounting

The Cooperative accounts for assets, liabilities, income, and expenses separately for each utility service furnished. Separate accounting is maintained for the gas department and the water department.

Recognition is given to all services rendered and facilities provided by each department, as well as those services provided by Graham County Electric Cooperative, Inc. under the operating and management agreement executed by both Cooperatives. These services are billed at predetermined rates. The accrual basis of accounting is followed in all departments.

Operating Revenues

Gas and water revenues are under the jurisdiction of the Arizona Corporation Commission.

The Cooperative records revenues as billed to the customers on a monthly basis. Revenue is not accrued for utility services delivered but not billed at the end of each month. The unbilled and unrecorded revenue at September 30, 2011 and 2010, was estimated to be \$46,978 and \$47,135, respectively, in the gas department and \$47,881 and \$51,039, respectively, in the water department.

The Cooperative's tariffs include an adjustment for flow-through of purchased natural gas costs. In order to match fuel costs and related revenues, costs billed in advance are recorded as overbilled consumers fuel cost and costs to be billed in the subsequent period are recorded as underbilled consumers fuel cost. For the years ended September 30, 2011 and 2010, the Cooperative was overbilled \$230,169 and \$378,378, respectively.

Group Concentration of Credit Risk

The Cooperative's headquarters is located in Pima, Arizona. The service area includes members located in Graham County, Arizona, and also includes retail service to the towns of Pima and Ft. Thomas, and wholesale services to Eden Water Company. The Cooperative records a receivable for gas and water service as billed on a monthly basis. The Cooperative requires a deposit from customers upon connection which is applied to any unpaid bills upon default. The deposit accrues interest annually at the rate of six percent. Deposits on hand totaled \$78,750 and \$77,625 at September 30, 2011 and 2010, respectively.

Patronage Capital Certificates

Patronage capital from associated organizations is recorded at the stated amount of the certificate.

-6-
GRAHAM COUNTY UTILITIES, INC.
NOTES TO FINANCIAL STATEMENTS

Inventories

Inventories which consist of construction materials and supplies are valued at average unit cost.

Cash and Cash Equivalents

For purposes of the statement of cash flows, cash and cash equivalents are represented by Cash – General.

Restricted Cash

As part of its agreement for loan funding from USDA Rural Development the Cooperative is required to accumulate a cash reserve fund. The fund balance at September 30, 2011 and 2010 was \$52,725 and \$46,648, respectively and was in compliance with funding requirements.

Federal Income Tax Status

The Cooperative qualifies for tax exempt status under Internal Revenue Code section 501(c)(12) with more than 85% of income consisting of amounts received from members.

On January 1, 2009, the Cooperative adopted the "uncertain tax positions" provisions of accounting principles generally accepted in the United States of America. The primary tax position of the Cooperative is its filing status as a tax exempt entity. The Cooperative determined that it is more likely than not that their tax positions will be sustained upon examination by the Internal Revenue Service (IRS), or other state taxing authority and that all tax benefits are likely to be realized upon settlement with taxing authorities.

The Cooperative files income tax returns in the U.S. federal jurisdiction. The Cooperative is no longer subject to U.S. federal and state income tax examinations by federal taxing authorities for years before 2008.

The Cooperative recognizes interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. There were no penalties or interest recognized during the years ended September 30, 2011 and 2010.

Allowance for Uncollectible Accounts

The Cooperative uses the aging method to allow for uncollectible accounts receivable. During the year, management makes an evaluation of past due accounts to determine collection ability. The accounts deemed uncollectible are written off upon approval by the Board of Directors.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

2. Assets Pledged

All assets are pledged as security for the long-term debt due the National Rural Utilities Cooperative Finance Corporation (CFC) and USDA.

3. Utility Plant and Depreciation

Utility plant is stated at the original cost of construction including the construction costs incurred by the utility from which the Cooperative acquired plant in November 1989. Original cost includes the cost of contracted services, direct labor, materials, and overhead reduced by contributions in aid to construction received in connection with new construction.

Maintenance and repairs including the renewal of minor items of plant not comprising a retirement unit are charged to the appropriate maintenance accounts.

Major classes of utility plant are summarized as follows:

	September 30,			
	2011			2010
	Gas	Water		
	Department	Department	Total	Total
Utility Plant in Service				
Intangible	\$ 42,522	\$ 37,708	\$ 80,230	\$ 80,230
Production		1,630,076	1,630,076	1,475,189
Transmission		1,098,561	1,098,561	1,098,561
Distribution	4,125,817	653,276	4,779,093	4,488,211
General	204,645	112,010	316,655	306,868
Land and Land Rights	1,416	22,507	23,923	23,923
Total Plant in Service	\$ 4,374,400	\$ 3,554,138	\$ 7,928,538	\$ 7,472,982
Construction Work in Progress	211,559	224,459	436,018	589,566
Utility Plant Acquisition				
Adjustment	415,484	610,168	1,025,652	1,025,652
Total Utility Plant	\$ 5,001,443	\$ 4,388,765	\$ 9,390,208	\$ 9,088,200

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GRAHAM COUNTY UTILITIES, INC.
NOTES TO FINANCIAL STATEMENTS

Provision has been made for depreciation on straight-line composite rates as follows:

	<u>Gas Department</u>	<u>Water Department</u>
Production		2.34% - 5.05%
Transmission		2.20% - 4.00%
Distribution		4.00% - 20.00%
Gas Mains	2.80%	
Services	4.10%	
Meters - Regulators	2.60%	
Structures	2.30%	
General	6.7% - 13.3%	10% - 20%

Depreciation accruals charged to expense for the periods ended September 30, 2011 and 2010, totaled \$235,603 and \$223,233, respectively.

A plant acquisition adjustment was created when the Cooperative purchased the assets and liabilities of City Utilities, Inc. and General Utilities, Inc. The acquisition adjustment, representing the amount of the purchase price over the book value of the net assets acquired, amounted to \$415,484 in the gas department and \$610,168 in the water department. Plant acquisition adjustments are amortizable over the estimated useful life of the plant acquired. The Cooperative has elected to amortize these costs over a 25-year period. The annual charge to expense is \$16,619 in the gas department and \$24,407 in the water department.

The plant acquisition costs and related provision for amortization at September 30, 2011, are summarized as follows:

	<u>Gas Department</u>	<u>Water Department</u>
Acquisition Adjustment	\$ 415,484	\$ 610,168
Less: Amortization		
Prior Periods	\$ 349,007	\$ 512,540
Current Year	16,619	24,407
	<u>\$ 365,626</u>	<u>\$ 536,947</u>
Unamortized Adjustment	<u>\$ 49,858</u>	<u>\$ 73,221</u>

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GRAHAM COUNTY UTILITIES, INC.
NOTES TO FINANCIAL STATEMENTS

4. Investments in Associated Organizations

Investments in associated organizations consisted of the following:

	September 30,	
	2011	2010
CFC		
Capital Term Certificates	\$ 205,692	\$ 128,049
Patronage Capital	101,245	93,924
Memberships	1,000	1,000
	<u>\$ 307,937</u>	<u>\$ 222,973</u>
Graham County Electric Cooperative, Inc.		
Patronage Capital	\$ 11,860	\$ 11,860
	<u>\$ 319,797</u>	<u>\$ 234,833</u>

5. Deferred Charges

Deferred charges consisted of the following:

	September 30,	
	2011	2010
Gas Department		
Unamortized Debt Expense	\$ 7,413	\$ 11,280
Other	9,980	9,777
	<u>\$ 17,393</u>	<u>\$ 21,057</u>
Water Department		
Unamortized Debt Expense	\$ 16,472	\$ 20,576
Other	9,223	9,155
	<u>\$ 25,695</u>	<u>\$ 29,731</u>
Total	<u>\$ 43,088</u>	<u>\$ 50,788</u>

During 1998, the Cooperative converted a CFC note to a lower interest rate of 7.1% for 15 years with a conversion fee of \$109,457. Amortization expense for the years ended September 30, 2011 and 2010, is \$7,971 and \$7,971, respectively.

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GRAHAM COUNTY UTILITIES, INC.
NOTES TO FINANCIAL STATEMENTS

6. Memberships

Memberships are comprised of the following:

	<u>September 30,</u>	
	<u>2011</u>	<u>2010</u>
Class A Memberships		
Graham County Electric Cooperative, Inc., entitled to one vote	\$ 5,000	\$ 5,000
Class B Memberships		
All qualified members of Graham County Electric Cooperative, Inc., \$5 membership fee, entitled to one vote per membership	21,627	21,689
Class C Memberships		
All others who receive service, \$5 membership fee, entitled to one vote per membership	<u>4,665</u>	<u>4,665</u>
	<u>\$ 31,292</u>	<u>\$ 31,354</u>

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

7. Accumulated Margins (Deficits)

This balance consists of net margins or (losses) as follows:

Calendar Year	Gas Department	Water Department	Total
1989	\$ 6,702	\$ (694)	\$ 6,008
1990	(14,127)	2,845	(11,282)
1991	(91,410)	(23,047)	(114,457)
1992	(41,115)	(13,851)	(54,966)
1993	(64,937)	5,077	(59,860)
1994	(46,268)	26,495	(19,773)
1995	(172,043)	(28,603)	(200,646)
1996	(68,293)	(3,409)	(71,702)
1997	(65,806)	(23,095)	(88,901)
1998	225,309	31,474	256,783
1999	97,405	62,256	159,661
2000	1,467	46,927	48,394
2001	39,062	40,741	79,803
2002	61,124	1,125	62,249
2003	(5,764)	69,524	63,760
2004	62,759	7,767	70,526
2005	92,446	47,242	139,688
2006	141,801	42,157	183,958
2007	69,003	36,636	105,639
2008	(179,686)	(26,292)	(205,978)
2009	(400,801)	(85,705)	(486,506)
2010	(239,276)	5,043	(234,233)
2011 Nine Months	83,594	20,358	103,952
	<u>\$ (508,854)</u>	<u>\$ 240,971</u>	<u>\$ (267,883)</u>
Patronage Capital Retired		(82,035)	(82,035)
	<u>\$ (508,854)</u>	<u>\$ 158,936</u>	<u>\$ (349,918)</u>

The Board of Directors has adopted the policy of separating each department's net gains or losses for allocation purposes. Patronage capital is allocated after all deficits have been recovered. During the years ended September 30, 2011 and 2010, no retirements of patronage capital were made.

Under the mortgage agreement with CFC, until the equities or margins equal or exceed 30% of the total assets of the Cooperative, the return to patrons of capital contributed by them is limited.

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GRAHAM COUNTY UTILITIES, INC.
NOTES TO FINANCIAL STATEMENTS

8. Mortgage Notes – CFC

Following is a summary of long-term debt due CFC maturing between September 30, 2014 and July 7, 2040:

	September 30,	
	2011	2010
Fixed - 7.10%	\$ 410,791	\$ 529,547
Fixed - 2.35% in 2011, 4.65% in 2010	139,907	182,393
Fixed - 7.45%	282,139	296,915
Fixed - 6.25%	342,858	351,250
Fixed - 7.00%	791,646	800,000
Fixed - 3.05%	244,751	250,000
	<u>\$ 2,212,092</u>	<u>\$ 2,410,105</u>
Less: Current Maturities	<u>210,000</u>	<u>197,000</u>
	<u><u>\$ 2,002,092</u></u>	<u><u>\$ 2,213,105</u></u>

Principal and interest installments on the above notes are due quarterly in amounts of approximately \$66,200. As of September 30, 2011, annual maturities of long-term debt due CFC for the next five years is as follows:

2012	\$ 210,000
2013	227,000
2014	240,000
2015	48,000
2016	50,000

The mortgages contain requirements requiring certain financial ratios to be maintained or exceeded. These requirements were not met during the years ended September 30, 2011 and 2010.

9. USDA Rural Development Note Payable

Following is a summary of long-term debt due USDA Rural Development:

	September 30,	
	2011	2010
5.000% Note Maturing March, 2032	\$ 133,600	\$ 137,260
4.500% Note Maturing August, 2035	236,737	242,152
4.500% Note Maturing July, 2040	83,540	84,931
4.125% Note Maturing March, 2047	1,056,918	1,069,923
	<u>\$ 1,510,795</u>	<u>\$ 1,534,266</u>
Less: Current Maturities	<u>24,400</u>	<u>23,500</u>
	<u><u>\$ 1,486,395</u></u>	<u><u>\$ 1,510,766</u></u>

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

Principal and interest installments on the above notes are due monthly in amounts of \$7,393. As of September 30, 2011, annual maturities of long-term debt due USDA Rural Development for the next five years are as follows:

2012	\$ 24,400
2013	25,600
2014	26,700
2015	27,900
2016	29,000

10. CIAC Refund Due

As a part of the final ruling by the Arizona Corporation Commission on recent rate cases for both the gas and water utilities the Cooperative agreed to refund contributions in aid of construction previously charged to the members. The total to be refunded is \$226,765 for the gas division and \$15,536 in the water division. The gas portion will be refunded over three years and is reflected in long term debt (\$88,151) and current maturities of long term debt (\$138,614). The water amount will be totally refunded in the next year and is reflected in Accounts Payable – Other.

11. Related Parties

The Cooperative is related by having substantially identical Boards of Directors and management with Graham County Electric Cooperative, Inc. (GCEC). GCEC provides administrative and general, management, operations, consumer accounting, and construction services to the Cooperative under an operating and management agreement signed by both parties on June 20, 1989.

GCEC is also the guarantor of the mortgage loan executed by the Cooperative to CFC.

Balances between the two Cooperatives are summarized as follows:

	September 30,	
	2011	2010
Graham County Utilities, Inc.		
Accounts Payable	\$ <u>(1,260,814)</u>	\$ <u>(834,642)</u>
Graham County Electric Cooperative, Inc.		
Accounts Receivable	\$ <u>1,260,814</u>	\$ <u>834,642</u>

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GRAHAM COUNTY UTILITIES, INC.
NOTES TO FINANCIAL STATEMENTS

12. Litigation and Contingencies

The Cooperative is not involved in any litigation that would materially affect the financial statements.

The Cooperative previously filed for rate increases in both water and gas companies with the Arizona Corporation Commission. During the prior period the rate cases were concluded and new rates were implemented in June 2010.

13. Subsequent Events

The Cooperative has evaluated subsequent events through November 22, 2011, the date the financial statements were available to be issued.

ACCOMPANYING INFORMATION

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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LUBBOCK, TEXAS 79423-1954

**INDEPENDENT AUDITORS' REPORT ON
ACCOMPANYING INFORMATION**

Our audits of the basic financial statements presented in the preceding section of this report were made for the purpose of forming an opinion on such financial statements taken as a whole. The accompanying information shown on pages 16 through 21 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

November 22, 2011

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GRAHAM COUNTY UTILITIES, INC.
GAS DEPARTMENT

Schedule 1

BALANCE SHEET
SEPTEMBER 30, 2011 AND 2010

ASSETS

	September 30,	
	2011	2010
UTILITY PLANT		
Plant in Service	\$ 4,374,400	\$ 4,095,366
Construction Work in Progress	211,559	366,322
Plant Acquisition Adjustment	415,484	415,484
	<u>\$ 5,001,443</u>	<u>\$ 4,877,172</u>
Less: Accumulated Provision for Depreciation and Amortization	2,509,706	2,353,251
	<u>\$ 2,491,737</u>	<u>\$ 2,523,921</u>
 OTHER PROPERTY AND INVESTMENTS AT COST OR STATED VALUE		
Investments in Associated Organizations	\$ 199,180	\$ 131,388
 CURRENT ASSETS		
Accounts Receivable (Less allowance for uncollectibles of \$64,981 in 2011 and \$70,453 in 2010)	\$ 44,253	\$ 20,842
Materials and Supplies	79,032	84,805
Other Current and Accrued Assets	23,205	26,747
Total Current Assets	<u>\$ 146,490</u>	<u>\$ 132,394</u>
 Deferred Charges	\$ 17,393	\$ 21,057
 TOTAL ASSETS	<u><u>\$ 2,854,800</u></u>	<u><u>\$ 2,808,760</u></u>

EQUITIES AND LIABILITIES

MEMBERS' EQUITY		
Memberships	\$ 28,792	\$ 28,854
Accumulated Margins (Deficits)	(508,854)	(542,878)
	<u>\$ (480,062)</u>	<u>\$ (514,024)</u>
 LONG -TERM DEBT		
CFC Mortgage Notes Less Current Maturities	\$ 1,583,883	\$ 1,709,163
CIAC Refunds Due	88,151	154,189
	<u>\$ 1,672,034</u>	<u>\$ 1,863,352</u>
 CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 263,244	\$ 188,906
Accounts Payable - Other	51,712	60,616
Accounts Payable - Graham County Electric Cooperative	985,487	699,527
Overbilled Consumers Fuel Cost	230,169	378,378
Accrued Taxes	34,294	34,846
Customers' Deposits and Prepayments	66,645	67,220
Accrued Interest	13,664	13,282
Accrued Payroll	17,613	16,657
Total Current Liabilities	<u>\$ 1,662,828</u>	<u>\$ 1,459,432</u>
 TOTAL EQUITIES AND LIABILITIES	<u><u>\$ 2,854,800</u></u>	<u><u>\$ 2,808,760</u></u>

**GRAHAM COUNTY UTILITIES, INC.
GAS DEPARTMENT**

Schedule 2

**STATEMENT OF INCOME AND ACCUMULATED MARGINS
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010**

	September 30,		Increase (Decrease)
	2011	2010	
OPERATING REVENUES			
Residential	\$ 2,273,160	\$ 2,380,373	\$ (107,213)
Irrigation	11,400	6,681	4,719
Commercial and Industrial	768,921	843,054	(74,133)
Fuel Cost Under (Over) Billed	148,828	24,648	124,180
Other Operating Revenues	40,043	(129,990)	170,033
Total Operating Revenues	<u>\$ 3,242,352</u>	<u>\$ 3,124,766</u>	<u>\$ 117,586</u>
OPERATING EXPENSES			
Purchased Gas	\$ 1,399,908	\$ 1,644,748	\$ (244,840)
Operations	374,592	303,884	70,708
Maintenance	328,460	283,816	44,644
Customer Accounts	327,997	306,437	21,560
Administrative and General	463,325	541,444	(78,119)
Depreciation and Amortization	156,455	145,705	10,750
Other Interest	47,571	62,047	(14,476)
Total Operating Expenses	<u>\$ 3,098,308</u>	<u>\$ 3,288,081</u>	<u>\$ (189,773)</u>
OPERATING MARGIN (DEFICIT) - Before Fixed Charges	<u>\$ 144,044</u>	<u>\$ (163,315)</u>	<u>\$ 307,359</u>
FIXED CHARGES			
Interest on Long-Term Debt	<u>121,332</u>	<u>82,985</u>	<u>38,347</u>
OPERATING MARGIN (DEFICIT) - After Fixed Charges	<u>\$ 22,712</u>	<u>\$ (246,300)</u>	<u>\$ 269,012</u>
Capital Credits	<u>11,312</u>	<u>8,050</u>	<u>3,262</u>
NET OPERATING MARGIN (DEFICIT)	<u>\$ 34,024</u>	<u>\$ (238,250)</u>	<u>\$ 272,274</u>
NONOPERATING MARGINS			
Interest	<u></u>	<u>388</u>	<u>(388)</u>
NET MARGIN (DEFICIT)	<u>\$ 34,024</u>	<u>\$ (237,862)</u>	<u>\$ 271,886</u>
ACCUMULATED DEFICIT - BEGINNING OF YEAR	<u>(542,878)</u>	<u>(305,016)</u>	
ACCUMULATED DEFICIT - END OF YEAR	<u>\$ (508,854)</u>	<u>\$ (542,878)</u>	

**GRAHAM COUNTY UTILITIES, INC.
GAS DEPARTMENT**

Schedule 3

**STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010**

	September 30,	
	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Margin (Deficit)	\$ 34,024	\$ (237,862)
Adjustments to Reconcile Net (Deficit) to Net Cash		
Provided by (Used in) Operating Activities		
Depreciation and Amortization	156,455	145,705
Capital Credits - Noncash	(5,655)	(4,025)
Deferred Charges	3,664	(5,509)
Over/(Under)billed Fuel Cost - Net	(148,209)	130,849
Accounts Receivable	(23,411)	704
Inventories and Other Current Assets	9,315	(13,974)
Payables and Accrued Expenses	(8,693)	(7,211)
Net Payments from - Graham County Electric Cooperative	285,960	(403,705)
Net Cash Provided by (Used in) Operating Activities	<u>\$ 303,450</u>	<u>\$ (395,028)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Gas Utility Plant	\$ (124,271)	\$ (522,607)
Investments in Associated Organizations	(62,137)	6,978
Net Cash Used in Investing Activities	<u>\$ (186,408)</u>	<u>\$ (515,629)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances on Long-Term Debt - CFC	\$	\$ 800,000
CIAC Refunds Due		226,765
Payments on Long-Term Debt - CFC	(116,980)	(101,776)
Payments on Long-Term Debt - Graham County Electric Cooperative		(14,607)
Memberships	(62)	275
Net Cash Provided by (Used in) Operating Activities	<u>\$ (117,042)</u>	<u>\$ 910,657</u>
CHANGE IN CASH	\$ 0	\$ 0
CASH - BEGINNING OF YEAR	<u>0</u>	<u>0</u>
CASH - END OF YEAR	<u><u>\$ 0</u></u>	<u><u>\$ 0</u></u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Paid During the Year for:		
Interest on Long-Term Debt	\$ 121,332	\$ 82,985
Federal Income Tax	<u>\$ 0</u>	<u>\$ 0</u>

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GRAHAM COUNTY UTILITIES, INC.
WATER DEPARTMENT

Schedule 4

BALANCE SHEET
SEPTEMBER 30, 2011 AND 2010

ASSETS

	September 30,	
	2011	2010
UTILITY PLANT AT COST		
Water Plant in Service	\$ 3,554,138	\$ 3,377,616
Construction Work in Progress	224,459	223,244
Plant Acquisition Adjustment	610,168	610,168
	<u>\$ 4,388,765</u>	<u>\$ 4,211,028</u>
Less: Accumulated Provision for Depreciation and Amortization	<u>2,162,798</u>	<u>2,042,624</u>
	<u>\$ 2,225,967</u>	<u>\$ 2,168,404</u>
 OTHER PROPERTY AND INVESTMENTS AT COST OR STATED VALUE		
Investments in Associated Organizations	\$ 120,617	\$ 103,445
 CURRENT ASSETS		
Cash - Restricted	\$ 52,725	\$ 46,648
Accounts Receivable - Customers (Less allowance for uncollectibles of \$12,012 in 2011 and \$14,091 in 2010)	40,278	19,319
Materials and Supplies	55,016	62,610
Other Current and Accrued Assets	7,572	8,916
Total Current Assets	<u>\$ 155,591</u>	<u>\$ 137,493</u>
 DEFERRED CHARGES	<u>\$ 25,695</u>	<u>\$ 29,731</u>
 NET ASSETS	<u>\$ 2,527,870</u>	<u>\$ 2,439,073</u>

EQUITIES AND LIABILITIES

EQUITY		
Memberships	\$ 2,500	\$ 2,500
Accumulated Margins	158,936	115,019
	<u>\$ 161,436</u>	<u>\$ 117,519</u>
 LONG-TERM DEBT		
CFC Mortgage Notes Less Current Maturities	\$ 418,209	\$ 503,942
USDA Rural Development Notes Less Current Maturities	1,486,395	1,510,766
	<u>\$ 1,904,604</u>	<u>\$ 2,014,708</u>
 CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 109,770	\$ 104,170
Accounts Payable - Other	30,399	21,483
Accounts Payable - Graham County Electric Cooperative	275,327	135,115
Accrued Taxes	23,159	23,453
Customers' Deposits and Prepayments	12,105	10,405
Accrued Interest	6,259	6,224
Accrued Payroll	4,811	5,996
Total Current Liabilities	<u>\$ 461,830</u>	<u>\$ 306,846</u>
 NET EQUITIES AND LIABILITIES	<u>\$ 2,527,870</u>	<u>\$ 2,439,073</u>

GRAHAM COUNTY UTILITIES, INC.
WATER DEPARTMENT

Schedule 5

STATEMENT OF INCOME AND ACCUMULATED MARGINS
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010

	September 30,		Increase (Decrease)
	2011	2010	
OPERATING REVENUES			
Residential	\$ 667,546	\$ 575,793	\$ 91,753
Commercial and Industrial	78,544	60,484	18,060
Sales for Resale	49,957	38,719	11,238
Other Operating Revenues	15,711	4,991	10,720
Total Operating Revenues	<u>\$ 811,758</u>	<u>\$ 679,987</u>	<u>\$ 131,771</u>
OPERATING EXPENSES			
Purchased Power - Pumping	\$ 54,478	\$ 49,922	\$ 4,556
Operations	65,188	64,972	216
Maintenance	217,199	180,383	36,816
Customer Accounts	81,216	63,484	17,732
Administrative and General	126,847	131,282	(4,435)
Depreciation and Amortization	120,174	118,555	1,619
Other Interest	13,762	17,236	(3,474)
Total Operating Expenses	<u>\$ 678,864</u>	<u>\$ 625,834</u>	<u>\$ 53,030</u>
OPERATING MARGINS - Before Fixed Charges	\$ 132,894	\$ 54,153	\$ 78,741
FIXED CHARGES			
Interest on Long-Term Debt	<u>92,387</u>	<u>91,923</u>	<u>464</u>
OPERATING MARGIN (DEFICIT) - After Fixed Charges	\$ 40,507	\$ (37,770)	\$ 78,277
Capital Credits	<u>3,333</u>	<u>8,653</u>	<u>(5,320)</u>
NET OPERATING MARGIN (DEFICIT)	\$ 43,840	\$ (29,117)	\$ 72,957
NONOPERATING MARGINS			
Interest	<u>77</u>	<u>69</u>	<u>8</u>
NET MARGIN (DEFICIT)	\$ 43,917	\$ (29,048)	\$ <u>72,965</u>
ACCUMULATED MARGINS - BEGINNING OF YEAR	<u>115,019</u>	<u>144,067</u>	
ACCUMULATED MARGINS - END OF YEAR	<u>\$ 158,936</u>	<u>\$ 115,019</u>	

**GRAHAM COUNTY UTILITIES, INC.
WATER DEPARTMENT**

Schedule 6

**STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010**

	September 30,	
	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Margin (Deficit)	\$ 43,917	\$ (29,048)
Adjustments to Reconcile Net (Deficit) to Net Cash		
Provided by Operating Activities		
Depreciation and Amortization	120,174	118,555
Capital Credits - Noncash	(1,667)	(1,460)
Deferred Charges	4,036	(5,051)
Accounts Receivable	(20,959)	(5,710)
Inventories and Other Current Assets	8,938	(1,199)
Payables and Accrued Expenses	9,172	16,028
Net Payments from (to) - Graham County Electric Cooperative	140,212	(101,813)
Net Cash Provided by (Used in) Operating Activities	\$ 303,823	\$ (9,698)
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Plant	\$ (177,737)	\$ (122,467)
Cash - Restricted	(6,077)	(69)
Investments in Associated Organizations	(15,505)	1,726
Net Cash Used in Investing Activities	\$ (199,319)	\$ (120,810)
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances on Long-Term Debt from CFC	\$	\$ 250,000
Payments on Note Payable to AEPCO		(25,667)
Payments on Long-Term Debt to CFC	(81,033)	(71,089)
Payments on Long-Term Debt to USDA	(23,471)	(22,736)
Net Cash Provided by (Used in) Financing Activities	\$ (104,504)	\$ 130,508
CHANGE IN CASH	\$ 0	\$ 0
CASH - BEGINNING OF YEAR	0	0
CASH - END OF YEAR	\$ 0	\$ 0
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Paid During the Year for:		
Interest on Long-Term Debt	\$ 92,387	\$ 91,923
Federal Income Tax	\$ 0	\$ 0

GRAHAM COUNTY UTILITIES, INC.

PIMA, ARIZONA

FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION

FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

**CERTIFIED PUBLIC ACCOUNTANTS
LUBBOCK, TEXAS**

GRAHAM COUNTY UTILITIES, INC.

PIMA, ARIZONA

FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION

FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

**GRAHAM COUNTY UTILITIES, INC.
PIMA, ARIZONA**

**FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION
FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009**

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BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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8215 NASHVILLE AVENUE

LUBBOCK, TEXAS 79423-1954

INDEPENDENT AUDITORS' REPORT

Board of Directors
Graham County Utilities, Inc.
Pima, Arizona

We have audited the accompanying balance sheets of Graham County Utilities, Inc. (the Cooperative), as of September 30, 2010 and 2009, and the related statements of income and accumulated margins, and cash flows for the years then ended. These financial statements are the responsibility of the Cooperative's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Graham County Utilities, Inc. as of September 30, 2010 and 2009, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 2, 2010, on our consideration of the Cooperative's internal control over financial reporting and on its compliance with certain provision of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

Bolinger, Segars, Gilbert & Moss L.L.P.

Certified Public Accountants

November 2, 2010

FINANCIAL STATEMENTS

GRAHAM COUNTY UTILITIES, INC.

Exhibit A

**BALANCE SHEET
FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009**

ASSETS

	September 30,	
	2010	2009
UTILITY PLANT		
Plant in Service	\$ 7,472,982	\$ 7,020,363
Construction Work in Progress	589,566	397,312
Plant Acquisition Adjustment	1,025,652	1,025,652
	<u>\$ 9,088,200</u>	<u>\$ 8,443,327</u>
Less: Accumulated Provision for Depreciation and Amortization	4,395,875	4,131,615
	<u>\$ 4,692,325</u>	<u>\$ 4,311,712</u>
OTHER PROPERTY AND INVESTMENTS		
Investments in Associated Organizations	\$ 234,833	\$ 238,052
CURRENT ASSETS		
Cash - General	\$ 46,648	\$ 46,579
Accounts Receivable (Less allowance for uncollectibles of \$84,544 in 2010 and \$92,362 in 2009)	40,161	35,155
Materials and Supplies	147,415	138,178
Other Current and Accrued Assets	35,663	29,727
Total Current Assets	<u>\$ 269,887</u>	<u>\$ 249,639</u>
DEFERRED CHARGES	<u>\$ 50,788</u>	<u>\$ 40,228</u>
TOTAL ASSETS	<u>\$ 5,247,833</u>	<u>\$ 4,839,631</u>

EQUITIES AND LIABILITIES

MEMBERS' EQUITY		
Memberships	\$ 31,354	\$ 31,079
Accumulated Margins (Deficits)	(427,859)	(160,949)
	<u>\$ (396,505)</u>	<u>\$ (129,870)</u>
LONG -TERM DEBT		
CFC Mortgage Notes Less Current Maturities	\$ 2,213,105	\$ 1,360,070
AEPSCO Note Payable Less Current Maturities		3,667
USDA Rural Development Note Payable Less Current Maturities	1,510,766	1,534,502
CIAC Refund Due	154,189	
	<u>\$ 3,878,060</u>	<u>\$ 2,898,239</u>
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 293,076	\$ 232,007
Accounts Payable - Other	82,099	81,476
Accounts Payable - Graham County Electric Coop	834,642	1,340,160
Overbilled Consumers Fuel Cost	378,378	247,529
Customers' Deposits and Prepayments	77,625	77,250
Accrued Taxes	58,299	57,317
Accrued Interest	19,506	19,199
Accrued Payroll	22,653	16,324
Total Current Liabilities	<u>\$ 1,766,278</u>	<u>\$ 2,071,262</u>
TOTAL EQUITIES AND LIABILITIES	<u>\$ 5,247,833</u>	<u>\$ 4,839,631</u>

See accompanying notes to financial statements.

GRAHAM COUNTY UTILITIES, INC.

Exhibit B

STATEMENT OF INCOME AND ACCUMULATED MARGINS
FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009

	September 30,	
	2010	2009
OPERATING REVENUES	\$ 3,804,753	\$ 4,034,707
OPERATING EXPENSES		
Purchased Gas	\$ 1,644,748	\$ 2,100,652
Power for Pumping	49,922	40,037
Operations	368,856	375,477
Maintenance	464,199	539,626
Consumer Accounts	369,921	342,675
Administrative and General	672,726	630,740
Depreciation and Amortization	264,260	282,852
Other Interest	79,283	69,033
Total Operating Expenses	\$ 3,913,915	\$ 4,381,092
OPERATING MARGINS (DEFICIT) - BEFORE FIXED CHARGES	\$ (109,162)	\$ (346,385)
Interest on Long-Term Debt	174,908	180,664
OPERATING (DEFICIT) - AFTER FIXED CHARGES	\$ (284,070)	\$ (527,049)
Capital Credits	16,703	9,951
NET OPERATING (DEFICIT)	\$ (267,367)	\$ (517,098)
NONOPERATING MARGINS		
Interest	457	608
NET (DEFICIT)	\$ (266,910)	\$ (516,490)
ACCUMULATED MARGINS - BEGINNING OF YEAR	(160,949)	355,541
ACCUMULATED MARGINS (DEFICIT) - END OF YEAR	\$ (427,859)	\$ (160,949)

See accompanying notes to financial statements.

GRAHAM COUNTY UTILITIES, INC.

Exhibit C

STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009

	September 30,	
	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net (Deficit)	\$ (266,910)	\$ (516,490)
Adjustments to Reconcile Net Margins to		
Net Cash Provided by Operating Activities		
Depreciation and Amortization	264,260	282,852
Capital Credits - Noncash	(5,485)	(11,951)
Over/(Under)billed Fuel Cost	130,849	279,946
Deferred Charges	(10,560)	(4,350)
Accounts Receivable	(5,006)	36,610
Inventories and Other Current Assets	(15,173)	6,796
Payables and Accrued Expenses	8,616	(53,304)
Net Payments (to) from - Graham County Electric Cooperative	(505,518)	522,467
Net Cash Provided by (Used in) Operating Activities	\$ (404,927)	\$ 542,576
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Plant	\$ (644,873)	\$ (315,580)
Investments in Associated Organizations	8,704	16,998
Net Cash Used in Investing Activities	\$ (636,169)	\$ (298,582)
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances on Long-Term Debt from CFC	\$ 1,050,000	\$
CIAC Refund Due	226,765	
Payments on Note Payable to AEPCO	(25,667)	(22,000)
Payments on Long-Term Debt to CFC	(172,865)	(157,329)
Payments on Long-Term Debt to GCEC	(14,607)	(41,728)
Payments on Long-Term Debt to USDA	(22,736)	(21,325)
Memberships	275	450
Net Cash Provided by (Used in) Financing Activities	\$ 1,041,165	\$ (241,932)
INCREASE (DECREASE) IN CASH	\$ 69	\$ 2,062
CASH - BEGINNING OF YEAR	46,579	44,517
CASH - END OF YEAR	\$ 46,648	\$ 46,579
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash Paid During the Year for:		
Interest on Long-Term Debt	\$ 174,908	\$ 179,621
Federal Income Tax	\$ 0	\$ 0

See accompanying notes to financial statements.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Graham County Utilities, Inc. (the Cooperative) is organized as a cooperative to provide gas and water utility services to customers in Graham County, Arizona. The Cooperative was incorporated February 14, 1989, and began operations in November, 1989, with the purchase of assets and liabilities from two private utility companies. The Cooperative has been granted exemption from Federal income taxes under Internal Revenue Code Section 501(c)(12).

Basis of Accounting

The Cooperative accounts for assets, liabilities, income, and expenses separately for each utility service furnished. Separate accounting is maintained for the gas department and the water department.

Recognition is given to all services rendered and facilities provided by each department, as well as those services provided by Graham County Electric Cooperative, Inc. under the operating and management agreement executed by both Cooperatives. These services are billed at predetermined rates. The accrual basis of accounting is followed in all departments.

Operating Revenues

Gas and water revenues are under the jurisdiction of the Arizona Corporation Commission.

The Cooperative records revenues as billed to the customers on a monthly basis. Revenue is not accrued for utility services delivered but not billed at the end of each month. The unbilled and unrecorded revenue at September 30, 2010 and 2009, was estimated to be \$47,135 and \$57,282, respectively, in the gas department and \$51,039 and \$39,691, respectively, in the water department.

The Cooperative's tariffs include an adjustment for flow-through of purchased natural gas costs. In order to match fuel costs and related revenues, costs billed in advance are recorded as overbilled consumers fuel cost and costs to be billed in the subsequent period are recorded as underbilled consumers fuel cost. For the years ended September 30, 2010 and 2009, the Cooperative was overbilled \$378,378 and \$247,529, respectively.

Group Concentration of Credit Risk

The Cooperative's headquarters is located in Pima, Arizona. The service area includes members located in Graham County, Arizona, and also includes retail service to the towns of Pima and Ft. Thomas, and wholesale services to Eden Water Company. The Cooperative records a receivable for gas and water service as billed on a monthly basis. The Cooperative requires a deposit from customers upon connection which is applied to any unpaid bills upon default. The deposit accrues interest annually at the rate of six percent. Deposits on hand totaled \$77,625 and \$77,250 at September 30, 2010 and 2009, respectively.

Patronage Capital Certificates

Patronage capital from associated organizations is recorded at the stated amount of the certificate.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

Inventories

Inventories which consist of construction materials and supplies are valued at average unit cost.

Cash and Cash Equivalents

For purposes of the statement of cash flows, cash and cash equivalents are represented by Cash – General.

Federal Income Tax Status

The Cooperative qualifies for tax exempt status under Internal Revenue Code section 501(c)(12) with more than 85% of income consisting of amounts received from members.

On January 1, 2009, the Cooperative adopted the "uncertain tax positions" provisions of accounting principles generally accepted in the United States of America. The primary tax position of the Cooperative is its filing status as a tax exempt entity. The Cooperative determined that it is more likely than not that their tax positions will be sustained upon examination by the Internal Revenue Service (IRS), or other state taxing authority and that all tax benefits are likely to be realized upon settlement with taxing authorities.

The Cooperative files income tax returns in the U.S. federal jurisdiction. The Cooperative is no longer subject to U.S. federal and state income tax examinations by federal taxing authorities for years before 2007.

The Cooperative recognizes interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. There were no penalties or interest recognized during the years ended September 30, 2010 and 2009.

Allowance for Uncollectible Accounts

The Cooperative uses the aging method to allow for uncollectible accounts receivable. During the year, management makes an evaluation of past due accounts to determine collection ability. The accounts deemed uncollectible are written off upon approval by the Board of Directors.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. Assets Pledged

All assets are pledged as security for the long-term debt due the National Rural Utilities Cooperative Finance Corporation (CFC) and USDA.

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GRAHAM COUNTY UTILITIES, INC.
NOTES TO FINANCIAL STATEMENTS

3. Utility Plant and Depreciation

Utility plant is stated at the original cost of construction including the construction costs incurred by the utility from which the Cooperative acquired plant in November 1989. Original cost includes the cost of contracted services, direct labor, materials, and overhead reduced by contributions in aid to construction received in connection with new construction.

Maintenance and repairs including the renewal of minor items of plant not comprising a retirement unit are charged to the appropriate maintenance accounts.

Major classes of utility plant are summarized as follows:

	September 30,			
	2010			2009
	Gas	Water		
	Department	Department	Total	Total
Utility Plant in Service				
Intangible	\$ 42,522	\$ 37,708	\$ 80,230	\$ 80,230
Production		1,475,189	1,475,189	1,475,189
Transmission		1,098,561	1,098,561	1,098,561
Distribution	3,856,570	631,641	4,488,211	4,036,149
General	194,858	112,010	306,868	306,311
Land and Land Rights	1,416	22,507	23,923	23,923
Total Plant in Service	\$ 4,095,366	\$ 3,377,616	\$ 7,472,982	\$ 7,020,363
Construction Work in Progress	366,322	223,244	589,566	397,312
Utility Plant Acquisition				
Adjustment	415,484	610,168	1,025,652	1,025,652
Total Utility Plant	\$ 4,877,172	\$ 4,211,028	\$ 9,088,200	\$ 8,443,327

Provision has been made for depreciation on straight-line composite rates as follows:

	Gas Department	Water Department
Production		2.34% - 5.05%
Transmission		2.20% - 4.00%
Distribution		4.00% - 20.00%
Gas Mains	2.80%	
Services	4.10%	
Meters - Regulators	2.60%	
Structures	2.30%	
General	6.7% - 13.3%	10% - 20%

Depreciation accruals charged to expense for the periods ended September 30, 2010 and 2009, totaled \$223,233 and \$241,826, respectively.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

A plant acquisition adjustment was created when the Cooperative purchased the assets and liabilities of City Utilities, Inc. and General Utilities, Inc. The acquisition adjustment, representing the amount of the purchase price over the book value of the net assets acquired, amounted to \$415,484 in the gas department and \$610,168 in the water department. Plant acquisition adjustments are amortizable over the estimated useful life of the plant acquired. The Cooperative has elected to amortize these costs over a 25-year period. The annual charge to expense is \$16,619 in the gas department and \$24,407 in the water department.

The plant acquisition costs and related provision for amortization at September 30, 2010, are summarized as follows:

	<u>Gas Department</u>	<u>Water Department</u>
Acquisition Adjustment	\$ 415,484	\$ 610,168
Less: Amortization		
Prior Periods	\$ 332,388	\$ 488,134
Current Year	16,619	24,407
	<u>\$ 349,007</u>	<u>\$ 512,541</u>
Unamortized Adjustment	<u>\$ 66,477</u>	<u>\$ 97,627</u>

4. Investments in Associated Organizations

Investments in associated organizations consisted of the following:

	<u>September 30,</u>	
	<u>2010</u>	<u>2009</u>
CFC		
Capital Term Certificates	\$ 128,049	\$ 137,512
Patronage Capital	93,924	93,414
Memberships	1,000	1,000
	<u>\$ 222,973</u>	<u>\$ 231,926</u>
Graham County Electric Cooperative, Inc.		
Patronage Capital	\$ 11,860	\$ 6,126
	<u>\$ 234,833</u>	<u>\$ 238,052</u>

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

5. Deferred Charges

Deferred charges consisted of the following:

	September 30,	
	2010	2009
Gas Department		
Unamortized Debt Expense	\$ 11,280	\$ 15,148
Other	9,777	400
	<u>\$ 21,057</u>	<u>\$ 15,548</u>
Water Department		
Unamortized Debt Expense	\$ 20,576	\$ 24,680
Other	9,155	
	<u>\$ 29,731</u>	<u>\$ 24,680</u>
Total	<u>\$ 50,788</u>	<u>\$ 40,228</u>

During 1998, the Cooperative converted a CFC note to a lower interest rate of 7.1% for 15 years with a conversion fee of \$109,457. Amortization expense for the years ended September 30, 2010 and 2009, is \$7,971 and \$8,983, respectively.

6. Memberships

Memberships are comprised of the following:

	September 30,	
	2010	2009
Class A Memberships		
Graham County Electric Cooperative, Inc., entitled to one vote	\$ 5,000	\$ 5,000
Class B Memberships		
All qualified members of Graham County Electric Cooperative, Inc., \$5 membership fee, entitled to one vote per membership	21,689	21,414
Class C Memberships		
All others who receive service, \$5 membership fee, entitled to one vote per membership	4,665	4,665
	<u>\$ 31,354</u>	<u>\$ 31,079</u>

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

7. Accumulated Margins (Deficits)

This balance consists of net margins or (losses) as follows:

Calendar Year	Gas Department	Water Department	Total
1989	\$ 6,702	\$ (694)	\$ 6,008
1990	(14,127)	2,845	(11,282)
1991	(91,410)	(23,047)	(114,457)
1992	(41,115)	(13,851)	(54,966)
1993	(64,937)	5,077	(59,860)
1994	(46,268)	26,495	(19,773)
1995	(172,043)	(28,603)	(200,646)
1996	(68,293)	(3,409)	(71,702)
1997	(65,806)	(23,095)	(88,901)
1998	225,309	31,474	256,783
1999	97,405	62,256	159,661
2000	1,467	46,927	48,394
2001	39,062	40,741	79,803
2002	61,124	1,125	62,249
2003	(5,764)	69,524	63,760
2004	62,759	7,767	70,526
2005	92,446	47,242	139,688
2006	141,801	42,157	183,958
2007	69,003	36,636	105,639
2008	(179,686)	(26,292)	(205,978)
2009	(400,801)	(85,705)	(486,506)
2010 Nine Months	(189,706)	(18,516)	(208,222)
	\$ (542,878)	\$ 197,054	\$ (345,824)
Patronage Capital Retired		(82,035)	(82,035)
	\$ (542,878)	\$ 115,019	\$ (427,859)

The Board of Directors has adopted the policy of separating each department's net gains or losses for allocation purposes. Patronage capital is allocated after all deficits have been recovered. During the year ended September 30, 2010 and 2009, no retirements of patronage capital were made.

Under the mortgage agreement with CFC, until the equities or margins equal or exceed 30% of the total assets of the Cooperative, the return to patrons of capital contributed by them is limited.

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GRAHAM COUNTY UTILITIES, INC.
NOTES TO FINANCIAL STATEMENTS

8. Mortgage Notes – CFC

Following is a summary of long-term debt due CFC maturing between September 30, 2014 and July 7, 2040:

	September 30,	
	2010	2009
Fixed - 7.10%	\$ 529,547	\$ 640,232
Fixed - 4.65%	182,393	222,961
Fixed - 7.45%	296,915	310,640
Fixed - 6.25%	351,250	359,137
Fixed - 7.00%	800,000	
Fixed - 3.05%	250,000	
	<u>\$ 2,410,105</u>	<u>\$ 1,532,970</u>
Less: Current Maturities	<u>197,000</u>	<u>172,900</u>
	<u>\$ 2,213,105</u>	<u>\$ 1,360,070</u>

Principal and interest installments on the above notes are due quarterly in amounts of approximately \$66,200. As of September 30, 2009, annual maturities of long-term debt due CFC for the next 5 years is as follows:

2011	\$ 197,000
2012	210,000
2013	227,000
2014	240,000
2015	48,000

The mortgages contain requirements requiring certain financial ratios to be maintained or exceeded. These requirements were not met during the year ended September 30, 2010 and 2009.

GRAHAM COUNTY UTILITIES, INC.

NOTES TO FINANCIAL STATEMENTS

\$15,536 in the water division. The gas portion will be refunded over three years and is reflected in long term debt (\$154,189) and current maturities of long term debt (\$72,576). The water amount will be totally refunded in the next year and is reflected in Accounts Payable – Other.

13. Related Parties

The Cooperative is related by having substantially identical Boards of Directors and management with Graham County Electric Cooperative, Inc. (GCEC). GCEC provides administrative and general, management, operations, consumer accounting, and construction services to the Cooperative under an operating and management agreement signed by both parties on June 20, 1989.

GCEC is also the guarantor of the mortgage loan executed by the Cooperative to CFC.

Balances between the two Cooperatives are summarized as follows:

	September 30,	
	2010	2009
Graham County Utilities, Inc.		
Accounts Payable	\$ (834,642)	\$ (1,340,164)
Note Payable		(14,607)
Net Due to Affiliated Cooperative	<u>\$ (834,642)</u>	<u>\$ (1,354,771)</u>
Graham County Electric Cooperative, Inc.		
Accounts Receivable	\$ 834,642	\$ 1,340,164
Note Receivable		14,607
Net Due from Affiliated Cooperative	<u>\$ 834,642</u>	<u>\$ 1,354,771</u>

14. Litigation and Contingencies

The Cooperative is not involved in any litigation that would materially affect the financial statements.

The Cooperative previously filed for rate increases in both water and gas companies with the Arizona Corporation Commission. During the current period the rate cases were concluded and new rates were implemented in June 2010.

15. Subsequent Events

The Cooperative has evaluated subsequent events through November 2, 2010, the date the financial statements were available to be issued.

ACCOMPANYING INFORMATION

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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**INDEPENDENT AUDITORS' REPORT ON
ACCOMPANYING INFORMATION**

Our audits of the basic financial statements presented in the preceding section of this report were made for the purpose of forming an opinion on such financial statements taken as a whole. The accompanying information shown on pages 15 through 20 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

November 2, 2010

-15-
GRAHAM COUNTY UTILITIES, INC.
GAS DEPARTMENT

Schedule 1

BALANCE SHEET
SEPTEMBER 30, 2010 AND 2009

ASSETS

	September 30,	
	2010	2009
UTILITY PLANT		
Plant in Service	\$ 4,095,366	\$ 3,743,276
Construction Work in Progress	366,322	195,805
Plant Acquisition Adjustment	415,484	415,484
	<u>\$ 4,877,172</u>	<u>\$ 4,354,565</u>
Less: Accumulated Provision for Depreciation and Amortization	2,353,251	2,207,546
	<u>\$ 2,523,921</u>	<u>\$ 2,147,019</u>
OTHER PROPERTY AND INVESTMENTS AT COST OR STATED VALUE		
Investments in Associated Organizations	\$ 131,388	\$ 134,341
CURRENT ASSETS		
Accounts Receivable (Less allowance for uncollectibles of \$70,453 in 2010 and \$76,885 in 2009)	\$ 20,842	\$ 21,546
Materials and Supplies	84,805	75,283
Other Current and Accrued Assets	26,747	22,295
Total Current Assets	<u>\$ 132,394</u>	<u>\$ 119,124</u>
Deferred Charges	\$ 21,057	\$ 15,548
TOTAL ASSETS	<u>\$ 2,808,760</u>	<u>\$ 2,416,032</u>

EQUITIES AND LIABILITIES

MEMBERS' EQUITY		
Memberships	\$ 28,854	\$ 28,579
Accumulated Margins (Deficits)	(542,878)	(305,016)
	<u>\$ (514,024)</u>	<u>\$ (276,437)</u>
LONG - TERM DEBT		
CFC Mortgage Notes Less Current Maturities	\$ 1,709,163	\$ 982,069
CIAC Refunds Due	154,189	
	<u>\$ 1,863,352</u>	<u>\$ 982,069</u>
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 188,906	\$ 159,807
Accounts Payable - Other	60,616	69,351
Accounts Payable - Graham County Electric Cooperative	699,527	1,103,232
Overbilled Consumers Fuel Cost	378,378	247,529
Accrued Taxes	34,846	36,220
Customers' Deposits and Prepayments	67,220	68,845
Accrued Interest	13,282	13,096
Accrued Payroll	16,657	12,320
Total Current Liabilities	<u>\$ 1,459,432</u>	<u>\$ 1,710,400</u>
TOTAL EQUITIES AND LIABILITIES	<u>\$ 2,808,760</u>	<u>\$ 2,416,032</u>

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GRAHAM COUNTY UTILITIES, INC.
GAS DEPARTMENT

Schedule 2

**STATEMENT OF INCOME AND ACCUMULATED MARGINS
FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009**

	September 30,		Increase (Decrease)
	2010	2009	
OPERATING REVENUES			
Residential	\$ 2,380,373	\$ 2,678,432	\$ (298,059)
Irrigation	6,681	8,456	(1,775)
Commercial and Industrial	843,054	976,257	(133,203)
Fuel Cost Under (Over) Billed	24,648	19,960	4,688
Other Operating Revenues	(129,990)	(280,168)	150,178
Total Operating Revenues	<u>\$ 3,124,766</u>	<u>\$ 3,402,937</u>	<u>\$ (278,171)</u>
OPERATING EXPENSES			
Purchased Gas	\$ 1,644,748	\$ 2,100,652	\$ (455,904)
Operations	303,884	309,874	(5,990)
Maintenance	283,816	376,161	(92,345)
Customer Accounts	306,437	283,581	22,856
Administrative and General	541,444	499,297	42,147
Depreciation and Amortization	145,705	137,095	8,610
Other Interest	62,047	54,993	7,054
Total Operating Expenses	<u>\$ 3,288,081</u>	<u>\$ 3,761,653</u>	<u>\$ (473,572)</u>
OPERATING (DEFICIT) - Before Fixed Charges	<u>\$ (163,315)</u>	<u>\$ (358,716)</u>	<u>\$ 195,401</u>
FIXED CHARGES			
Interest on Long-Term Debt	<u>82,985</u>	<u>79,858</u>	<u>3,127</u>
OPERATING (DEFICIT) - After Fixed Charges	<u>\$ (246,300)</u>	<u>\$ (438,574)</u>	<u>\$ 192,274</u>
Capital Credits	<u>8,050</u>	<u>7,229</u>	<u>821</u>
NET OPERATING (DEFICIT)	<u>\$ (238,250)</u>	<u>\$ (431,345)</u>	<u>\$ 193,095</u>
NONOPERATING MARGINS			
Interest	<u>388</u>	<u>546</u>	<u>(158)</u>
NET (DEFICIT)	<u>\$ (237,862)</u>	<u>\$ (430,799)</u>	<u>\$ 192,937</u>
ACCUMULATED MARGINS - BEGINNING OF YEAR	<u>(305,016)</u>	<u>125,783</u>	
ACCUMULATED MARGINS (DEFICIT) - END OF YEAR	<u>\$ (542,878)</u>	<u>\$ (305,016)</u>	

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GRAHAM COUNTY UTILITIES, INC.
GAS DEPARTMENT

Schedule 3

STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009

	September 30,	
	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net (Deficit)	\$ (237,862)	\$ (430,799)
Adjustments to Reconcile Net (Deficit) to Net Cash		
Provided by (Used in) Operating Activities		
Depreciation and Amortization	145,705	137,095
Capital Credits - Noncash	(4,025)	(9,229)
Deferred Charges	(5,509)	3,467
Over/(Under)billed Fuel Cost - Net	130,849	279,946
Accounts Receivable	704	35,674
Inventories and Other Current Assets	(13,974)	14,051
Payables and Accrued Expenses	(7,211)	(19,624)
Net Payments from - Graham County Electric Cooperative	(403,705)	352,481
Net Cash Provided by (Used in) Operating Activities	<u>\$ (395,028)</u>	<u>\$ 363,062</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Gas Utility Plant	\$ (522,607)	\$ (239,405)
Investments in Associated Organizations	6,978	10,481
Net Cash Used in Investing Activities	<u>\$ (515,629)</u>	<u>\$ (228,924)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances on Long-Term Debt - CFC	\$ 800,000	\$
CIAC Refunds Due	226,765	
Payments on Long-Term Debt - CFC	(101,776)	(92,860)
Payments on Long-Term Debt - Graham County Electric Cooperative	(14,607)	(41,728)
Memberships	275	450
Net Cash Provided by (Used in) Operating Activities	<u>\$ 910,657</u>	<u>\$ (134,138)</u>
INCREASE (DECREASE) IN CASH	\$ 0	\$ 0
CASH - BEGINNING OF YEAR	<u>0</u>	<u>0</u>
CASH - END OF YEAR	<u><u>\$ 0</u></u>	<u><u>\$ 0</u></u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Paid During the Year for:		
Interest on Long-Term Debt	\$ 82,985	\$ 82,630
Federal Income Tax	<u>0</u>	<u>0</u>

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GRAHAM COUNTY UTILITIES, INC.
WATER DEPARTMENT

Schedule 4

BALANCE SHEET
SEPTEMBER 30, 2010 AND 2009

ASSETS

	September 30,	
	2010	2009
UTILITY PLANT AT COST		
Water Plant in Service	\$ 3,377,616	\$ 3,277,087
Construction Work in Progress	223,244	201,507
Plant Acquisition Adjustment	610,168	610,168
	<u>\$ 4,211,028</u>	<u>\$ 4,088,762</u>
Less: Accumulated Provision for Depreciation and Amortization	<u>2,042,624</u>	<u>1,924,069</u>
	<u>\$ 2,168,404</u>	<u>\$ 2,164,693</u>
 OTHER PROPERTY AND INVESTMENTS AT COST OR STATED VALUE		
Investments in Associated Organizations	\$ 103,445	\$ 103,711
 CURRENT ASSETS		
Cash - General	\$ 46,648	\$ 46,579
Accounts Receivable - Customers (Less allowance for uncollectibles of \$14,091 in 2010 and \$15,477 in 2009)	19,319	13,609
Materials and Supplies	62,610	62,895
Other Current and Accrued Assets	8,916	7,432
Total Current Assets	<u>\$ 137,493</u>	<u>\$ 130,515</u>
 DEFERRED CHARGES	<u>\$ 29,731</u>	<u>\$ 24,680</u>
 NET ASSETS	<u>\$ 2,439,073</u>	<u>\$ 2,423,599</u>

EQUITIES AND LIABILITIES

EQUITY		
Memberships	\$ 2,500	\$ 2,500
Accumulated Margins	115,019	144,067
	<u>\$ 117,519</u>	<u>\$ 146,567</u>
 LONG-TERM DEBT		
CFC Mortgage Notes Less Current Maturities	\$ 503,942	\$ 378,001
AEPKO Notes Payable Less Current Maturities	3,667	3,667
USDA Rural Development Notes Less Current Maturities	1,510,766	1,534,502
	<u>\$ 2,014,708</u>	<u>\$ 1,916,170</u>
 CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 104,170	\$ 72,200
Accounts Payable - Other	21,483	12,125
Accounts Payable - Graham County Electric Cooperative	135,115	236,928
Accrued Taxes	23,453	21,097
Customers' Deposits and Prepayments	10,405	8,405
Accrued Interest	6,224	6,103
Accrued Payroll	5,996	4,004
Total Current Liabilities	<u>\$ 306,846</u>	<u>\$ 360,862</u>
 NET EQUITIES AND LIABILITIES	<u>\$ 2,439,073</u>	<u>\$ 2,423,599</u>

GRAHAM COUNTY UTILITIES, INC.
WATER DEPARTMENT

Schedule 5

STATEMENT OF INCOME AND ACCUMULATED MARGINS
FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009

	September 30,		Increase (Decrease)
	2010	2009	
OPERATING REVENUES			
Residential	\$ 575,793	\$ 546,737	\$ 29,056
Commercial and Industrial	60,484	50,027	10,457
Sales for Resale	38,719	31,186	7,533
Other Operating Revenues	4,991	3,820	1,171
Total Operating Revenues	<u>\$ 679,987</u>	<u>\$ 631,770</u>	<u>\$ 48,217</u>
OPERATING EXPENSES			
Purchased Power - Pumping	\$ 49,922	\$ 40,037	\$ 9,885
Operations	64,972	65,603	(631)
Maintenance	180,383	163,465	16,918
Customer Accounts	63,484	59,094	4,390
Administrative and General	131,282	131,443	(161)
Depreciation and Amortization	118,555	145,757	(27,202)
Other Interest	17,236	14,040	3,196
Total Operating Expenses	<u>\$ 625,834</u>	<u>\$ 619,439</u>	<u>\$ 6,395</u>
OPERATING MARGINS - Before			
Fixed Charges	\$ 54,153	\$ 12,331	\$ 41,822
FIXED CHARGES			
Interest on Long-Term Debt	<u>91,923</u>	<u>100,806</u>	<u>(8,883)</u>
OPERATING (DEFICIT) - After Fixed Charges	<u>\$ (37,770)</u>	<u>\$ (88,475)</u>	<u>\$ 50,705</u>
Capital Credits	<u>8,653</u>	<u>2,722</u>	<u>5,931</u>
NET OPERATING (DEFICIT)	<u>\$ (29,117)</u>	<u>\$ (85,753)</u>	<u>\$ 56,636</u>
NONOPERATING MARGINS			
Interest	<u>69</u>	<u>62</u>	<u>7</u>
NET (DEFICIT)	<u>\$ (29,048)</u>	<u>\$ (85,691)</u>	<u>\$ 56,643</u>
ACCUMULATED MARGINS - BEGINNING OF YEAR	<u>144,067</u>	<u>229,758</u>	
ACCUMULATED MARGINS - END OF YEAR	<u>\$ 115,019</u>	<u>\$ 144,067</u>	

GRAHAM COUNTY UTILITIES, INC.
WATER DEPARTMENT

Schedule 6

STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2010 AND 2009

	September 30,	
	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net (Deficit)	\$ (29,048)	\$ (85,691)
Adjustments to Reconcile Net (Deficit) to Net Cash		
Provided by Operating Activities		
Depreciation and Amortization	118,555	145,757
Capital Credits - Noncash	(1,460)	(2,722)
Deferred Charges	(5,051)	(7,817)
Accounts Receivable	(5,710)	936
Inventories and Other Current Assets	(1,199)	(7,255)
Payables and Accrued Expenses	16,028	(33,680)
Net Payments from (to) - Graham County Electric Cooperative	(101,813)	169,986
Net Cash Provided by (Used in) Operating Activities	\$ (9,698)	\$ 179,514
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Plant	\$ (122,467)	\$ (76,175)
Investments in Associated Organizations	1,726	6,517
Net Cash Used in Investing Activities	\$ (120,741)	\$ (69,658)
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances on Long-Term Debt from CFC	\$ 250,000	\$
Payments on Note Payable to AEPCO	(25,667)	(22,000)
Payments on Long-Term Debt to CFC	(71,089)	(64,469)
Payments on Long-Term Debt to USDA	(22,736)	(21,325)
Net Cash Provided by (Used in) Financing Activities	\$ 130,508	\$ (107,794)
INCREASE IN CASH	\$ 69	\$ 2,062
CASH - BEGINNING OF YEAR	46,579	44,517
CASH - END OF YEAR	\$ 46,648	\$ 46,579
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Paid During the Year for:		
Interest on Long-Term Debt	\$ 91,923	\$ 96,991
Federal Income Tax	\$ 0	\$ 0